

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

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|------------------------------------|---|------------------------|
| Avista Corporation, |) | |
| Bonneville Power Administration, |) | |
| Idaho Power Company, |) | |
| The Montana Power Company, |) | |
| Nevada Power Company, |) | Docket No. RT01-35-000 |
| PacifiCorp, |) | |
| Portland General Electric Company, |) | |
| Puget Sound Energy, Inc., |) | |
| Sierra Pacific Power Company. |) | |

COMMENTS OF THE
ENERGY DIVISION
OF THE
WASHINGTON OFFICE OF TRADE AND ECONOMIC DEVELOPMENT

INTRODUCTION

1. The Energy Division of the Washington Office of Trade and Economic Development (OTED) is pleased to offer these comments regarding the RTO West compliance filing by Avista Corporation, Bonneville Power Administration, Idaho Power Company, Montana Power Company, Nevada Power Company, PacifiCorp, Portland

General Electric Company, Puget Sound Energy, Inc., and Sierra Pacific Power Company (Filing Utilities), pursuant to Order No. 2000. The Energy Division has a longstanding interest in regional transmission issues. Energy Division staff have participated as a Commission Class member of both the Northwest and Western Regional Transmission Associations, in the development of the IndeGO proposal for a Northwest independent system operator, and in the public process leading up to the recommendation of the Regional Representatives Group (RRG) to the filing utilities and, ultimately, to the filing commented on here.

2. OTED wishes to congratulate the filing utilities on a well-designed and productive public process. Considering the extremely short time frame in which to develop a proposal, the lingering divisions in the region resulting from the IndeGO process, the diversity of utility structures and the widely varying levels of retail restructuring from one state to another, the proposal and the process that led up to it greatly exceeded our expectations. OTED supports a great deal of the ideas in the filing, and looks forward to a continuing public process to supply the detail that will be needed for the Stage 2 filing.

3. The filing utilities have asked the Commission for a declaratory order with respect to certain of the documents that are contained in the filing. OTED's comments will be organized around these requests.

OTED INTEREST IN REGIONAL TRANSMISSION RESTRUCTURING

4. The OTED Energy Division's participation in regional transmission institutions is rooted in its mission to facilitate the inclusion of public interest criteria into state,

regional, and national energy policy. OTED's criteria for protecting the public interest in transmission system operation and expansion include:

- Ensuring that the interstate transmission grid is operated reliably;
- Facilitating efficient, competitive wholesale power markets;
- Sending meaningful price signals for efficient operation and expansion of the transmission grid;
- Ensuring that non-transmission alternatives, such as demand-side management and distributed generation, are treated equivalently to transmission solutions in the planning and grid expansion processes;
- Ensuring the equitable treatment of intermittent renewable generation in operational protocols and planning and expansion processes;
- Retaining the value of the existing system for the loads that have paid for its construction; and
- Facilitating public involvement in major decisions regarding the planning and operation of the region's transmission system;

ARTICLES OF INCORPORATION AND BYLAWS

5. OTED generally supports the proposed governance structure and Bylaws. Specifically, OTED believes that the independent Board of Trustees, with the broad business experience required by the trustee qualifications, will meet FERC's requirements for independence. We also believe that the open stakeholder advisory committee outlined in the Bylaws is a significant improvement over earlier proposals that would have assigned a formal "gatekeeper" role to a limited-membership committee that would have taken formal votes. Such a structure would have compromised the

independence of the Board by investing the advisory committee with both a formal role in Board processes and an excessive degree of moral authority. The proposal ensures the independence of the Board by properly constraining the role of the advisory committee to simply giving advice to the Board on matters that it may address.

6. OTED finds the Bylaws inadequate in the following areas:

7. Lack of an adequate mission or purpose statement:

According to Article III of the Bylaws, the purposes of RTO West “*are to serve as an RTO for the RTO West Geographic Area in accordance with the applicable requirements of FERC, including but not limited to the applicable requirements of FERC with respect to RTO characteristics and functions;...*” (Bylaws p. 8, article III) While this is technically what is required of RTO West per Order 2000, one hopes that an organization on which so much effort is being expended has more purpose than simply to fulfill a regulatory mandate. The RTO Board of Trustees will be called upon again and again to exercise its discretion to decide which among competing economic and non-economic interests should take precedence with respect to a particular action. Additional guidance to the Trustees as to the mission of the organization in their trust may be of assistance as they struggle to interpret the mission of RTO West. We recommend the following:

“The purposes of the corporation are to serve the public interest by reliably operating the high-voltage transmission system of the RTO West Geographic Area in accordance with the applicable requirements of FERC, including but not limited to requirements with respect to RTO characteristics and functions; by ensuring that operations of additions to the high-voltage transmission system of the RTO West Geographic Area occur at the least cost to society, including externalities; and by carefully balancing the various economic and non-economic interests as represented by the members of the corporation in all of its day-to-day decisions;...”

8. Absence of agreed-upon role for the manager of the market monitoring unit:

To ensure that this pivotal function has the independence it needs to critically evaluate decisions made by the staff and officers of RTO West, the role and authorities of the market monitoring unit and the appointment of the manager directly by the board must be provided for in the Bylaws. This institutional framework was agreed to by the RRG, but for some reason is absent from the documents that were filed on October 16.

9. Excessively high fee for membership in RTO West:

Public interest groups and representatives of residential and small commercial customers have expressed concern about the \$1000 annual membership fee. The RTO Board should be given the authority to waive or reduce the fee to ensure that legitimate voices of public interest groups and small customers can be represented through RTO membership. Many of these groups have a long history of constructive participation in state and regional energy policy forums, including the public process leading up to this filing, and it would be a great loss to the region and to the RTO if these voices were absent or silenced within the RTO membership.

10. Lack of provision for access by state agencies to confidential RTO data:

In the Bylaws Article VI, Section 4 the following language should be added: *“Provide information to energy, regulatory and enforcement agencies of states, provinces and the federal government, as requested. If information is deemed confidential by the RTO or the parties supplying the information to the RTO, such information shall be supplied upon agency agreement to maintain its confidentiality.”* State agencies must have access to operational and price data in order to evaluate the efficiency and effectiveness of wholesale power markets, to make policy decisions related to energy facility siting and

regulation of retail electric service, and to otherwise protect the public interest and fulfill their statutory duties. Concerns about confidentiality are unfounded; state agencies routinely collect confidential data from companies, and state law generally provides for severe legal penalties for unauthorized disclosure of confidential data.

SCOPE AND CONFIGURATION OF RTO WEST

11. Proposed scope and configuration sufficient

OTED concurs with the filing utilities that the scope and regional configuration of RTO West as proposed is sufficient to achieve most of the potential benefits of RTO formation. However, the Commission should reserve the right to revisit this issue should one or more of the filing utilities opt not to join RTO West. Additionally, the Commission should encourage RTO West to make every effort to achieve participation by Canadian utilities and to work closely with other RTOs and control area operators that are not RTO members to eliminate barriers to trade at the boundaries.

12. Common congestion management model needed for western interconnection

The filing utilities have not asked this Commission to make any determinations with respect to the congestion management and ancillary service proposals. Nevertheless, we believe that Commission action at this time could greatly enhance the likelihood that a single, market-based mechanism for managing congestion could be developed for application by the three RTOs in the western interconnection. The Commission noted in its in November 1 Order on the California market that:

California is physically integrated into an extensive interstate transmission grid and has therefore been part of a western electricity market for a long time. California's markets will never realize optimal performance until the impediments to efficient utilization of the regional transmission grid are eliminated and the

regional interstate transmission system is designed in such a way that it supports transparent, competitive Western bulk power markets - - markets that support all of the wholesale products that California requires, markets that remove impediments to efficient imports and exports, markets that eliminate rate pancaking and allow California to access more distant markets at a lower cost, markets that undertake regional transmission planning to ensure that the needs of California are considered when transmission expansions in other states are considered, and markets that allow regional market hubs like Palo Verde to develop where new generation can be located to serve multi-state markets. . . .

(San Diego Gas & Electric Co. v. Sellers of Energy and Ancillary Services Into Markets Operated by the California Independent System Operator and the California Power Exchange, Docket No. EL00-95-000, et al. (November 1, 2000) at 46.)

13. As the Commission notes, the western interconnection functions largely as a single market, and long-distance trading of power has been common in the west for many years, both to take advantage of the seasonal diversity of loads and resources that exists in the west, and more recently to seek out greater profits in shorter-term markets. These markets have developed without many of the problems with loop flow and line overloads that have plagued the east. What has made these markets possible is the west's existing system of physical transmission rights.

14. As this past summer's events demonstrated, the existing system is far from perfect. The west's "rated system path" method of scheduling transmission is inaccurate. Transmission rate pancaking presents continued barriers to increased trading in the west. And neither congestion nor loop flow are managed according to market principles. Order 2000 requires RTOs to address each of these areas, and all three nascent RTOs in the west have taken tentative steps to do so. However, they have not yet done so in the coordinated manner that is necessary to preserve and enhance the benefits of existing wholesale trade in the west. It would be a supreme irony if the formation of RTOs,

intended to enhance the competitiveness of wholesale power markets, instead served to erect barriers to trade that did not previously exist in the west.

15. The most promising way to prevent that is to establish a common system of flow-based, physical transmission rights throughout the western interconnection. RTO West's proposal for a flow-based physical rights model for managing congestion achieved widespread, though not universal, support during the collaborative process. Desert STAR has also proposed a flow-based physical rights model, and the California ISO has considered this model in its ongoing comprehensive market reform process. Locational marginal pricing with financial transmission rights may be theoretically more optimal, but physical rights match up better with the physical and institutional structures that exist in the west. The west is characterized by dense load and generation centers connected by long lines, which may allow a zonal pricing system to approximate the theoretical perfection of a nodal system.

16. Physical rights have other advantages that are attractive to an industry in varying states of transition to retail access. Physical rights models do not require a mandatory centralized dispatch of all generators in the region. This allows utilities that provide bundled, regulated retail service to continue to dispatch their own generation to serve their own load, much as they always have. Physical rights allow for the self-provision of almost all ancillary services, which will enable utilities to minimize their exposure to volatile wholesale market prices. Physical rights allow owners of multiple hydroelectric projects to decide for themselves how to optimize water flow and comply with project license requirements, and they allow for easier retention of cooperative arrangements such as the Pacific Northwest Coordination Agreement that have provided the region

with a great deal of benefit over the years through coordinated operation of Columbia River dams. Finally, and perhaps most importantly, physical rights do not require the negotiation of elaborate protocols between neighboring RTOs for managing congestion at RTO boundaries.

17. The Commission indicated in Order 2000 that it would allow a certain period of time for experimentation with various methods of managing congestion before requiring that a single method be implemented throughout the country:

While our experience has shown that, in specific situations, some approaches to congestion pricing appear to have advantages over others, we have not yet identified one approach as being clearly superior to all others. Furthermore, the Commission recognizes that an RTO's choice of a congestion pricing method will depend on a variety of factors, many of which may be unique to that RTO. Therefore, we will allow RTOs considerable flexibility to propose a congestion pricing method that is best suited to each RTO's individual circumstances.

(Regional Transmission Organizations, Docket No. RM99-2-000; Order No. 2000, (December 20, 1999), at 390.)

18. However, the Commission's California order appears to contain an implicit preference for nodal pricing:

The current congestion management system is fundamentally flawed and needs to be overhauled or replaced. This market redesign is crucial for providing transmission schedules that are based on physical reality and accurate price signals for the siting of new generation. Therefore we will require that the proposal, at a minimum, include a meaningful number of zones that significantly address congestion on the system. In this regard, we also require that the proposal provide a comparison with a nodal energy price proposal (i.e. locational marginal prices for each bus or node on the grid).

(San Diego Gas & Electric Co. v. Sellers of Energy and Ancillary Services Into Markets Operated by the California Independent System Operator and the California Power Exchange, Docket No. EL00-95-000, et al. (November 1, 2000) at 31.)

19. We hope the California experience has not caused the Commission to reconsider its commitment to allow experimentation. We believe that a common system of flow-based, physical transmission rights throughout the western interconnection shows the most promise for building on the existing institutions and expanding trade throughout the west. Among other things, such a system must have:

- A common scheduling model, which means that any generation-to-load schedule must be deemed by each RTO in the west to flow on the same flow paths in any given hour;
- Common methods for determining transfer capability on each side of an RTO boundary, and protocols that do not require the user to purchase two sets of rights to use the same path;
- Common scheduling timelines, including use-it-or-lose-it deadlines for transmission rights and pre-schedule cut-off times;
- Common settlement periods, and agreements between neighboring control areas for settling inadvertent energy interchange at the real-time price of energy; and
- Common definitions for widely-used terms, so that Firm Transmission Rights, Recalable Transmission Rights, or Non-firm Transmission Rights don't carry different priorities in different RTOs.

20. Western states have been persistent advocates of ensuring that multiple transmission system operators in the west facilitate trade across system boundaries. Western state comments on the proposed RTO rule suggested that the Commission review western RTO proposals together to ensure that “seams issues” were adequately

addressed. This is more critical than ever. The Commission should ensure not only that the commercial models being adopted by the three RTOs are not incompatible, but that they will ultimately lead to a single system for reserving transmission across the entire interconnection. A single, westwide RTO may be out of reach, but there is no reason to give up on a single market structure.

21. Implementing this goal may require that existing timetables for developing congestion management protocols be altered, or that processes currently underway be broadened to include stakeholders throughout the west. While we recognize the urgency of the problems in California, we believe that consumers throughout the west, including those in California, will ultimately be better served by a single, competitive wholesale power market throughout the western interconnection.

TRANSMISSION OPERATING AGREEMENT

22. Bonneville, PacifiCorp, and Idaho Power have asked the Commission to issue a declaratory order finding that the “concepts as a package” embodied in the Transmission Operating Agreement (TOA) are acceptable and consistent with the requirements of Order 2000. OTED believes it is premature to issue such an order. Parties in the region need to be able to see all the documents that describe RTO duties and responsibilities, and the rights of other parties vis-à-vis the RTO, before they can make informed judgements as to whether any one of the documents is acceptable. The Commission should wait until the Stage 2 filing to rule on the acceptability of the TOA.

23. We note two areas in particular where we believe the TOA is incomplete.

24. Granting of firm transmission rights (Section 15)

The agreement on the disposition of existing transmission rights is an agreement of the filing utilities only, and does not represent a consensus agreement among regional stakeholders. The proposed method for granting firm transmission rights (FTRs) to incumbent utilities for “Pre-Existing Transmission Agreements”, “Load Service Obligations”, and, potentially, “Non-Converted Transmission Agreements” would lock up large portions of the transmission grid for the sole use of incumbent utilities. Utilities would be granted time-variant FTRs for up to 48 dispatches in a single year, leaving them largely immune to the need for seasonal and hourly shaping of transmission rights, while competitors would be required to assemble the rights they need to make firm power sales from whatever is left over. Such dispatches need not be simultaneously feasible; the TOA contains protocols for reducing rights in the event of over-allocation of a flowpath. Nor is the protection limited to historic uses; utilities would be granted rights for load growth, up to the entire capacity of a flowpath.

25. OTED is concerned that the current proposal could short-circuit the proposed market mechanism for congestion management, which relies on a robust bilateral market to ration scarce grid capacity among market participants. If FTRs are too thinly traded in secondary markets, generators and loads will not receive meaningful price signals regarding their usage of the transmission system, and the goals of a market mechanism will be thwarted. The Commission will need to carefully review the proposal to ensure that it will provide sufficient liquidity in secondary FTR markets to satisfy the requirements of Order 2000:

...congestion pricing proposals should seek to ensure that (1) the generators that are dispatched in the presence of transmission

constraints are those that can serve system loads at least cost, and
(2) limited transmission capacity is used by market participants
that value that use most highly.

(Regional Transmission Organizations, Docket No. RM99-2-000;
Order No. 2000, (December 20, 1999), at 382.)

26. We recognize that there is an inherent tension between protecting existing uses of the grid such as bundled retail service and making transmission available to facilitate a competitive wholesale generation market, and we remain committed to the notion that retail loads must retain the benefits of the transmission systems for which they have paid through bundled retail rates. We also recognize the need for utilities to retain the rights they need to fulfill existing contracts and provide bundled retail service to customers still under state regulation.

27. However, we believe that a mechanism can be designed that will accomplish both goals. A variety of proposals were discussed during the public process; one promising mechanism would require each utility to place its protected FTRs into an annual auction, but allow it to set an arbitrarily high reserve price to ensure it can keep the FTRs for which there is truly no substitute, while targeting the revenues of the auctions back to the loads that are paying the utility's company rate. We encourage the filing utilities to continue to explore mechanisms such as this one that would introduce greater liquidity into the FTR market, while capturing the scarcity value of the existing system for the customers that are paying its fixed costs.

28. Planning (Sections 11 and 12)

Section 11 of the TOA outlines a number of obligations of the ETO "*in support of upgrades or expansions to the Transmission Facilities determined by RTO West to be needed*" (TOA Section 11.1 at 35), including:

- *“To the extent permitted by applicable law, cooperate with RTO West in connection with the obtaining of necessary siting and other permits and licenses.”* (TOA Section 11.1.2 at 36)
- *“To the extent permitted by applicable law, take necessary and appropriate steps, which if and to the extent necessary would include (1) exercising its eminent domain authority, (2) taking appropriate regulatory and judicial actions to condemn the necessary rights-of-way for such upgrades or expansions...”* (TOA Section 11.1.3 at 36)

29. OTED believes that it is inappropriate to require the ETO to take these steps without an explicit requirement for RTO West to undertake a least-cost planning process. Planning and expansion of transmission facilities has traditionally been done by vertically integrated utilities for the purpose of providing bundled retail service at the least total cost, under the supervision of state commissions and local boards. While a planning process that looks beyond traditional utility boundaries to considers grid-wide needs offers the potential to improve upon the existing process, such improvement is considerably less likely if the RTO does not plan the grid according to least-cost principles.

30. An acceptable least-cost planning process would include a determination of whether the project would provide significant economic benefits over alternatives such as generation and demand-side management, and would include an explicit analysis of the external costs, such as environmental degradation, of each of the alternatives. If RTO West found that non-transmission projects provided

comparable benefits at lower costs to society, RTO West would refrain from requiring the actions listed above from transmission owners.

31. There should also be a requirement that ETOs follow least-cost planning principles for ETO-planned projects that are to be included in company rates. Some sort of oversight role for RTO West may also be appropriate, with a focus on ensuring that RTO West is not placed in the position of seeking to recover through load-based access fees the costs of facilities that have not met least-cost tests. There is no such requirement in the TOA as it currently exists. Even worse, RTO West appears to be explicitly prohibited from engaging in such a process if a project is proposed by TransConnect:

RTO West shall retain primary planning responsibility and final decision-making authority with respect to RTO West Controlled Transmission Facilities; provided that if the additions, modifications and expansions to such facilities do not impair reliability or bulk transmission capability of the RTO West Transmission System, the requested approval of RTO West shall not be unreasonably delayed or withheld. (TOA Section 12.1.2 at 38)

32. The description of the planning process in Attachment P does little to clarify the roles of RTO West, the ETO, and others in planning and financing grid expansion projects. Until further detail is added to the RTO West planning and grid expansion processes, the Commission should not approve the planning language in Sections 11 and 12 of the TOA.

33. Supremacy of TOA over other RTO documents

The filing utilities intend the TOA to be the governing document in the event of any conflict among the various documents that govern RTO actions. This is also important to state commissions — the TOA is the document that will prescribe

the transfer of assets from the utilities to the RTO and hence is the document over which state commissions will retain jurisdictional authority. We do not fundamentally disagree with this notion. In fact, we believe that the TOA is the appropriate document in which to nail down the money flows that are necessary to prevent cost shifting. However, there may be details in the October 16 version of the TOA that are better left to the Board, especially considering that changes in the TOA will require bilateral negotiations between RTO West and each of the nine filing utilities, plus regulatory approval by up to seven state commissions, in addition to this Commission. Before approving the TOA, the Commission should very carefully consider whether the TOA is too specific and takes too much discretion from the RTO Board outside of the areas where specificity is needed to protect state interests.

CONCLUSION

33. OTED thanks the Commission for the opportunity to submit these comments, and looks forward to continuing to work with the filing utilities and other stakeholders on the formation of RTO West.

Respectfully submitted on November 20, 2000:

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